MCPU
Exhibit 1.0R

REBUTTAL TESTIMONY

OF

DAN E. LONG
(On Behalf of Mt. Carmel Public Utility CO.)

SUPPORTING TARIFFS

FOR

RESIDENTIAL DELIVERY SERVICE

ILLINOIS COMMERCE COMMISSION
DOCKET Nos. 01-0525/01-0625

Rebuttal Testimony of
Dan E. Long
On Behalf of
Mt. Carmel Public Utility Co.

<u>WITNESS IDENTIFICATION</u>

Q. Please state your name and business address.

A. My name is Dan Long. I am a partner with SPI Energy Group. My business address is 2621 Montega, Suite D, Springfield, Illinois 62704.

Q. Did you previously submit testimony in the above referenced dockets?

A. Yes.

Q. What is the purpose of your rebuttal testimony?

A. My rebuttal testimony is intended to respond to the testimony submitted by various Commission Staff witnesses as well as present revised exhibits containing revenue requirements and proposed rates.

Q. Would you describe the documents that make up your Rebuttal Testimony?

A. Yes. Exhibit 1.0R is the rebuttal testimony itself. Accompanying the testimony are exhibits 4.0R and 5.0R. Exhibit 4.0R is a revised calculation of the residential delivery service rates, adjusted for the revenue requirement changes proposed by Mr. Smith, and adopting the rate design proposed by Mr. Hendrickson. Exhibit 5.0R is a revised version of the electric embedded cost of service study. The Total Company Delivery Service revenue requirement has been adjusted for the revenue requirement changes proposed by Mr. Smith. The resulting allocation of costs to the residential class forms the basis for the revenue requirement from which residential delivery service rates are calculated on Exhibit 4.0R.

Direct Testimony of Sheena Kight

Q. What is the basic purpose of Ms. Kight's testimony?

A. In ICC Staff Exhibit 1.0 Ms. Kight presents her evaluation of the capital structure and overall rate of return required by Mt. Carmel in providing electric delivery services.

Q. In filing its proposed tariffs for residential delivery services, what cost of capital and rate of return were used by Mt. Carmel?

A. Mt. Carmel utilized a capital structure and rate of return identical to that proposed by Ms. Kight in her testimony.

Q. Does the use of an identical set of values indicate Mt. Carmel's acceptance of the Staff recommendation and the underlying analysis whose results are the basis for that recommendation?

A. Not entirely. Mt. Carmel believes that, for the specific purposes encompassed in these dockets, Staff's recommended values are reasonable. Mt. Carmel does, however, stop just short of endorsing the specific analysis that was used to develop these values.

Q. Would you explain why the Company does not agree with the analysis?

A. Yes. For several years, the appearance and actual composition of the utility industry in general has been changing, especially in Illinois. Mt. Carmel has been unique among this group for some time. With the development and implementation of the deregulation of electric service in Illinois, Mt. Carmel has become even more unique. Mt. Carmel has been for some time the smallest "stand alone" combination utility in Illinois. Of late, not only is Mt. Carmel the smallest investor owned utility in Illinois but, Mt. Carmel is the only Illinois utility that is both based and owned within Illinois. In addition, Mt. Carmel has no unregulated affiliates or subsidiaries nor any non-regulated activities within the utility, and has no parent company owner. This makes the selection and use of a sample for purposes of developing capital costs difficult for anyone, Staff included. While the testimony that follows does not agree with the method used by Staff in evaluating Mt. Carmel, the Company does understand that to a certain extent the Staff is somewhat limited in how it might evaluate a utility such as Mt. Carmel. And, while it is easy for the Company to disagree with Staff's methodology, at this point in time the Company has no suggestion for a replacement analysis. Rather, by airing the following comments, the Company would like to begin a process whereby in subsequent proceedings the Staff and Company may have already developed a mechanism to evaluate Mt. Carmel that is more fitting to the Company's unique nature.

Mt. Carmel believes that the type of sample used by Staff in this proceeding is no longer a good basis for comparison, for several reasons. First, all of the sample companies are many magnitudes larger than Mt. Carmel. Second, not all sample companies even offer delivery services since their respective states have yet to implement deregulation. Third, none of the sample companies purchases all of its power requirements from outside suppliers.

I believe that the type of sample used is inappropriate for additional reasons. Ms. Kight, on page three, beginning at line 53 states, " Since Mt. Carmel does not have market-traded common stock, DCF and risk premium models cannot be applied directly to Mt. Carmel; therefore, I applied both models to a sample of integrated electric utility companies."

The sample companies have common stock that is traded publicly and freely by investors. As Ms. Kight has observed, Mt. Carmel's stock is not freely traded. This leads me to believe that the public, or market perception of the stock of the sample companies as potential investments is different than the perception of potential investors in a company such as Mt. Carmel. It also leads me to believe that a different type and set of investors not only invests in Mt. Carmel, but they invest in Mt. Carmel for different reasons, and with different expectations than investors who may buy stock in the publicly traded sample companies for which an active and liquid market exists.

On page four of her testimony, Ms. Kight explains how various companies were culled from a larger group to obtain the sample. Companies were removed if their revenues from electric service were less than 70% of total revenues. I am uncertain how this improves the comparability to Mt. Carmel, as I stated before that I don't believe that the remaining sample companies all provide delivery services.

Ms. Kight also excludes companies whose Standard & Poors published debt rating is less than A-. Mt. Carmel is not rated by Standard & Poors. As a result, while all remaining sample companies may be similar in their S&P rating, they differ from Mt. Carmel, who is not rated.

Next, Ms. Kight removed companies for whom IBES and Zacks did not publish long-term growth rates. While all remaining sample companies presumably have published growth rates by IBES and Zacks, Mt. Carmel does not. For this particular qualification, the excluded companies may have more in common with Mt. Carmel than those that remained part of the sample.

Q. Is there any part of the Staff analysis other than the sample that you believe is not appropriately applied to, or comparable to, Mt. Carmel?

A. Yes. I believe that Staff has incorrectly imputed adjustments to Mt. Carmel's capital structure. Ms. Kight correctly establishes that Mt. Carmel's cost of debt is 8.5%. However, on page 23, beginning on line 416, she states, "Electric utilities that share Mt. Carmel's implied A credit rating have a mean total debt ratio of 53.29%."

First, I would point out that, of the utilities observed by Ms. Kight, only Mt. Carmel has an "implied" credit rating. Second, the type of debt instrument available to, and utilized by Mt. Carmel is different from that used by the sample, and by the industry in general. The industry in general typically acquires long-term debt in the form of publicly traded bond issuances. These bonds require an annual interest payment, but the utility issuing the bonds pays, over the term of the bond life, only debt service, or interest. The issuing utility retains the use of the borrowed capital, as part of its capital structure, over the life of the bond issue. This results in a relatively stable level of debt for the utility, given no major change in total debt. And, given no change in common equity shares outstanding, the debt ratio is also relatively stable. Mt. Carmel, because of its relatively low level of capital requirements, does not have access to capital available by issuing publicly traded bonds. Mt. Carmel's current debt is in the form of a simple interest bank loan. While the typical utility has borrowed capital available for use over the term of its bond issue, Mt. Carmel repays its borrowed capital throughout the term of the loan. This makes their common equity ratio appear lower at the outset of a new loan, and higher at the end of the loan's term, as the apparent debt ratio moves in the reverse direction. During this period, common stock outstanding may not have changed at all. The table on page 23 of Ms. Kight's testimony demonstrates this effect. Between 1998 and 2000, Mt. Carmel's debt ratio appears to fall. One would normally assume that some shift in common equity is taking place, or that bond issues have been retired. In fact, as the debt ratio for Mt. Carmel falls, it is because the Company's debt principal is being repaid, thereby reducing the debt capital available for use by the company until such time as it is retired, and a new loan is established. As debt is repaid, the Company must rely increasingly on either current income, retained earnings or shareholder equity for capital requirements. As a result, the capital structure that Ms. Kight is attempting to modify is really the appropriate measure of the only capital available to the Company over time.

Direct Testimony of Thomas Q. Smith

Q. What is the basic purpose of Mr. Smith's testimony?

A. Mr. Smith, through ICC Staff Exhibit 2.0, proposes adjustments to the Company's operating income statements.

Q. Does the Company object to or disagree with the adjustments proposed by Mr. Smith?

A. No. For purposes of this proceeding, the Company believes Mr. Smith's adjustments are reasonable.

Q. What is the overall impact of the adjustments proposed by Mr. Smith?

A. Staff Exhibit 2.0, Schedule 2.1 shows the impact of Mr. Smith's proposed adjustments. The proposed adjustments have the effect of reducing the delivery services revenue requirement by $263,476. Operating expenses are also reduced by $263,476, leaving net operating income equal to that proposed by Mt. Carmel in its original filing. The end result is a 5.34% reduction in revenue, with overall return on rate base remaining unchanged at 10.75%. This yields a net operating income of $990,485.

Q. Has the Company chosen to incorporate Mr. Smith's proposed changes?

A. Yes. Attached to my Rebuttal Testimony is Exhibit 5.0R, which is the embedded electric cost of service analysis for electric delivery services. The column titled "Total Current Electric Adjusted Costs" now reflects the adjustments proposed by Mr. Smith. The column titled "Proposed Residential DST Revenue Requirement" has been reduced in proportion to the adjustments to Total Delivery Services revenue requirement. The Residential Delivery Service Revenue Requirement has been reduced by $126,903. The impact of this will be discussed in the portion of my Rebuttal Testimony that responds to the Direct Testimony of John Hendrickson.

Direct Testimony of John W. Hendrickson

Q. What is the purpose of Mr. Hendrickson's testimony?

A. Mr. Hendrickson, in ICC Staff Exhibit 3.0, states that he agrees with the way in which the Company's cost of service study allocates costs to the residential delivery service class. He proposes that if the revenue requirement proposed by the Company were to be changed, his recommendation would be to keep the Customer Charge at the level proposed by the Company and to modify the Energy Charge to conform to the adjusted revenue requirement.

Q. Has the Company accepted and adopted Mr. Hendrickson's recommendation?

A. Yes. Attached to my Rebuttal Testimony is Exhibit 4.0R that incorporates Mr. Hendrickson's proposal.

Q. Would you describe Exhibit 4.0R?

A. Exhibit 4.0R is a revised calculation of the residential delivery service rates similar to Exhibit 4.0 that was filed with my direct testimony. Exhibit 4.0R utilizes the adjusted delivery service revenue requirement for the residential class that appears on Exhibit 5.0R. Exhibit 5.0R also presents a modified adjustment amount for uncollectable expenses. This adjustment results from the change in the level of the residential delivery service revenue requirement. When the class revenue requirement was adjusted downward as a result of the adjustments made by Mr. Smith, it was necessary to calculate a different uncollectable expense associated with the lower residential delivery service class revenue requirement. This adjustment is shown on Exhibit 4.0R. Exhibit 4.0R, in adopting Mr. Hendrickson's recommendation, maintains the Customer Charge at the $5.21 level, and calculates an associated energy charge of $0.03487. Assuming the Commission accepts Staff's adjustments and the resulting revenue requirement for residential delivery service, Mt. Carmel would file tariff sheets in the form of the exhibits filed with its direct testimony, as modified for the price levels stated above.

Direct Testimony of Dr. Eric P. Schlaf

Q. What is the purpose of Dr. Schlaf's testimony?

A. Dr. Schlaf's testimony (ICC Staff Exhibit 4.0) reviews the Company's Terms and Conditions of Delivery Service, Mt. Carmel's Residential Delivery Service Implementation Plan, and makes a recommendation regarding the use of "electronic signatures" obtained by suppliers to satisfy Letter of Agency ("LOA") requirements.

Q. Have you reviewed Dr. Schlaf's proposal that suppliers should be allowed to obtain LOA signatures electronically over the internet?

A. Yes. The Company's Terms and Conditions of Delivery Service, referred to by Dr. Schlaf, states in part that "the letter must be signed and dated by the Customer….". The definition does not state implicitly or explicitly that the signature must be of the "wet" variety discussed by Dr. Schlaf. If the Commission decides that LOA's obtained with electronic signatures should be accepted by utilities, Mt. Carmel will not need to modify any of its tariffs because its tariffs, in their current form do not specifically preclude such acceptance. This matter is a legal issue that deals with the relationship between the ARES and the Customer. I give no opinion on this matter.

Q. Does this conclude your testimony?

A. Yes it does.